

Message Text

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ACTION ARA-14

INFO OCT-01 ISO-00 AID-05 CIAE-00 COME-00 EB-08 FRB-03

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SP-02 LAB-04 SIL-01 OMB-01 NSC-05 SS-15 STR-04

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FM AMEMBASSY LIMA

TO SECSTATE WASHDC PRIORITY 6032

INFO AMEMBASSY QUITO

AMEMBASSY SANTIAGO

AMEMBASSY CARACAS

AMEMBASSY LA PAZ

AMEMBASSY BOGOTA

C O N F I D E N T I A L LIMA 6573

E.O. 11652: GDS

TAGS: EGEN, EFIN, PE

SUBJECT: SOLVING THE FINANCIAL CRISIS: SOME SPECULATION

REF: A) LIMA 6511; B) LIMA 6387; C) LIMA 6379

SUMMARY: PERU IS NOW STRUGGLING TO AVOID OUTRIGHT DEFAULT ON SEVERAL PAST-DUE INTERNATIONAL OBLIGATIONS. INSOFAR AS WE KNOW, THESE EFFORTS HAVE BEEN SUCCESSFUL TO DATE. MEANWHILE, THOUGH SOME PERUVIANS CONTINUE TO SEEK UNLIKELY SOLUTIONS TO FINANCIAL CRISIS, WE BELIEVE THAT BEST WAY OUT OF PRESENT CRISIS IS SUCCESSFUL STANDBY NEGOTIATION WITH IMF. HOWEVER, GIVEN POLITICAL REALITIES AND POTENTIAL FOR FURTHER POPULAR UNREST HERE, WE WONDER WHETHER GOP FEELS IT CAN UNDERTAKE THE SORT OF MEASURES WHICH PRESUMABLY WOULD BE REQUIRED TO OBTAIN IMF STANDBY. IF IN GOP JUDGMENT THE COUNTRY IS NOT YET READY FOR SUCH STERN MEASURES, THEN GOVERNMENT IS LEFT WITH NEXT-BEST ALTERNATIVE OF MAKING ONLY PRO FORMA APPROACH TO IMF, FOLLOWED BY EARLY APPEAL TO DEBTOR BANKS FOR STRETCHOUT OF
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LOAN PAYMENTS. END SUMMARY

1. EMBASSY ECON COUNSELOR HAS MET RECENTLY WITH A NUMBER OF PERSONS FROM PERUVIAN FINANCIAL CIRCLES AND REPRESENTATIVES OF FOREIGN BANKS IN PERU. THERE IS A CLEAR CONSENSUS WITHIN THIS GROUP THAT PERU HAS NOW GONE BEYOND THE POINT WHERE ITS INTERNATIONAL RESERVES ARE SUFFICIENT TO MEET CURRENT FOREIGN

OBLIGATIONS. THE IMPRESSION IS THAT THE GOP (I.E. CENTRAL BANK AND BANCO DE LA NACION) IS NOW ENGAGED IN THUS-FAR SUCCESSFUL SCRAMBLE TO AVOID DEFAULTS BY OBTAINING SHORT-TERM EXTENSIONS ON SEVERAL LOANS COMING DUE.

2. SOME OF THE SPECIFIC CASES CITED ARE OUTSTANDING OBLIGATIONS TO AT LEAST ONE THE STEERING COMMITTEE BANKS IN NEW YORK WHICH ARRANGED LAST YEAR'S BALANCE-OF-PAYMENTS LOAN, A LEADING GERMAN BANK, THE ECUADOREAN STATE OIL COMPANY (QUITO 5053, NOTAL), AND A JAPANESE FINANCIAL INSTITUTION. REPORTEDLY ALL HAVE THUS FAR AGREED TO NEGOTIATE POSSIBLE PAYMENT DEFERRALS, THOUGH OF COURSE WE CANNOT BE CERTAIN THAT THESE NEGOTIATIONS WILL BE SUCCESSFUL.

3. GIVEN THE GRAVITY OF THE CURRENT FINANCIAL SITUATION, IT IS NOT SURPRISING THAT CONCERNED PERUVIANS ARE LOOKING AT A WIDE RANGE OF POSSIBLE SOLUTIONS. THERE IS ONE REPORT THAT A MYSTERIOUS MR.SPECK, A LOS ANGELES MONEY BROKER, IS OFFERING BY MEANS OF A TELEX ALLEGEDLY SENT TO EVERY MEMBER OF THE CABINET, SOME \$3 BILLION IN READY CASH (OBTAINED THROUGH ARAB SOURCES) TO TIDE PERU OVER. MR. SPECK IS REPORTEDLY IN LIMA AT THIS VERY MOMENT. AS EMBASSY HAS INDICATED PREVIOUSLY (LIMA 6227) WE GIVE LITTLE CREDENCE TO POSSIBILITY THAT ANY LARGE SUM WILL BE FORTHCOMING FROM SUCH A SOURCE.

4. ANOTHER STORY GIVEN FAIRLY WIDE CIRCULATION IS THAT
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HAYA DE LA TORRE, IN EXCHANGE FOR POLITICAL CONTROL BY APRA OVER THE CONSTITUENT ASSEMBLY WHICH WILL FRAME THE NEW PERUVIAN CONSTITUTION, WILL ATTEMPT TO PREVAIL UPON PRESIDENT CARLOS ANDRES PEREX OF VENEZUELA TO MAKE AN IMMEDIATE GOV LOAN OF \$150 MILLION TO THE PERUVIAN CENTRAL BANK. GIVEN THE POLITICAL REALITIES IN VENEZUELA, WE ALSO DOUBT THAT SUBSTANTIAL SUMS WILL BE FORTHCOMING FROM THAT SOURCE.

5. PERHAPS A MORE REASONABLE SCENARIO, THOUGH IT, TOO, HAS SOME PROBLEMS, HAS BEEN SUGGESTED BY ONE OF PIAZZA'S TOP ECONOMIC ADVISERS WHO HAS KEPT VERY CLOSEPQN TOUCH WITH THE NEW ECONOMIC TEAM. HE SUGGESTS THAT THE PIECE-MEAL MEASURES (REF A), DESIGNED TO PLACATE THE WORKING CLASS, WILL CONTINUE FOR TWO WEEKS OR SO, FOLLOWED BY SOME PUBLIC ANNOUNCEMENT (POSSIBLY BY FINANCE MINISTER) OF RENEWED AUSTERITY MEASURES, PERHAPS INCLUDING A FIRM PLEDGE TO HOLD DOWN THE PUBLIC SECTOR DEFICIT, AND A SUBSTANTIAL DEVALUATION. (SOURCE MENTIONED 40 BILLION SOLES AS POSSIBLE PUBLIC SECTOR DEFICIT GOAL, AND NEW EXCHANGE RATE OF ABOUT 95 TO THE DOLLAR, WHICH SEEM, RESPECTIVELY, UNREALISTIC AND UNDULY DRASTIC TO US.)

IN ANY CASE, GOP WOULD HOPE THAT THE NEW AUSTERITY MEASURES WOULD PROVIDE THE BASIS FOR REOPENING DISCUSSIONS WITH THE IMF. IF THIS PROVED TO BE THE CASE, THEN PRESIDENT OF CENTRAL BANK AND JOSE LUIS BROUSSET, PRESIDENT OF BANCO POPULAR, WOULD VISIT WASHINGTON IN EARLY SEPTEMBER TO PLEAD PERU'S CASE FOR A STANDBY WITH THE WITTEVEEN AT THE FUND. IF A STANDBY IS OBTAINED, PERUVIANS BELIEVE THAT NEGOTIATIONS WITH COMMERCIAL BANKS WOULD BE LIKELY TO PROSPER. WE SEE AS MOST SERIOUS PROBLEMS WITH THIS SCENARIO THE PAST RELUCTANCE OF POWERFUL CABINET FIGURES, EG. GEN. IBANEZ O'BRIEN, TO AGREE TO EARLY DEVALUATION, AND GENERAL CONCERN WITHIN THE COUNCIL OF MINISTERS WITH POSSIBLE ADVERSE POPULAR REACTION TO THE ANNOUNCEMENT OF NEW AUSTERITY MEASURES AT THIS TIME.
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6. ANOTHER REAL POSSIBILITY IS THAT GOP OFFICIALS WILL CONTINUE PIECEMEAL PROGRAM OF ECONOMIC MEASURES FOLLOWED BY PRO FORMA APPROACH FOR STANDBY AND (IN ABSENCE OF MEANINGFUL NEW AUSTERITY MEASURES) A TURNDOWN BY IMF. GOP WOULD THEN TURN TO STEERING COMMITTEE AND OTHER CREDITOR BANKS, ASKING THEM FOR A RESCHEDULING WHICH WOULD PERMIT A SHORT-TERM DEFERRAL ON THE PAYMENT OF OUTSTANDING OBLIGATIONS WITH THE HOPE THAT, WITH IMPORTS TIGHTLY RESTRICTED AND SOME IMPROVEMENT IN EXPORTS, PERU WOULD BE BETTER ABLE TO MEET ITS OBLIGATIONS AT SOME POINT IN THE NEAR FUTURE. IN THIS CASE BANKS WOULD BE FACED WITH CHOICE OF ALLOWING PERU TO DEFAULT OR AGREEING TO RESCHEDULING, AND WOULD PRESUMABLY TAKE THE SECOND ALTERNATIVE.

7. WHILE OUR CLEAR PREFERENCE WOULD BE FOR THE PERUVIANS, IN THEIR OWN LONG-RANGE BEST INTEREST, TO COME UP WITH A PROGRAM ACCEPTABLE TO THE IMF AND PROCEED TO SUCCESSFUL STANDBY NEGOTIATIONS, IT SEEMS POSSIBLE AT THE MOMENT THAT, GIVEN THE POLITICAL CONSTRAINTS AND POTENTIAL FOR FURTHER POPULAR UNREST HERE, THE GOVERNMENT WILL FEEL THAT IT MUST OPT FOR THE SCENARIO OUTLINED IN PARAGRAPH 6, ABOVE. SHLAUDEMAM

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